UNIT 9 FOREIGN EXCHANGE REGULATIONS AND TAXATION ISSUES

Objectives

After goring through this unit you would be able to understand:

- the basis of international tax system and the various types of taxes
- the meaning of tax havens
- international tax strategy
- modes of double taxation relief
- indian tax system
- foreign exchange management act

Structure

9.1 INTRODUCTION

Taxation is one of the core variables for various financial decisions such as international investment decisions, international working capital decisions, fund raising decisions, and decisions regarding dividend and other payments. These decisions become more complex when we take into consideration the multiple tax jurisdictions and tax rates which the multinational corporation faces. Secondly the varying tax rates.

The international tax system should be neutral, equitable and avoid double taxation. Tax neutrality implies that the tax structure should not be an impediment in optimal allocation of capital among different countries. If tax is neutral the investments will move from the countries with lower returns to countries with higher returns. Tax neutrality may be explained in terms of capital export neutrality and capital import neutrality. Capital export neutrality means that the rates of taxes should be same between domestic investment and foreign investment, which implies that the pre and past tax return is same between a capital exporting and capital importing country. The uniformity of this kind is difficult to achieve because of differences in accounting policies and tax rates of different countries.

Capital-import neutrality on the other hand occurs, when a uniform tax rate is applied

Capital-import neutrality on the other hand occurs, when a uniform tax rate is applied to all firms competing in the same capital importing country. The result of this type of neutrality is the lack of competitive advantage for either domestic or foreign firms in context of tax rates.

Tax equity means that all similarly situated tax payers should participate in the cost of operating the government according to the same rules. The concept of tax equity can be interpreted in two ways, one is that the contribution of each tax payer should be proportionate to the quantum of public services used by the tax payer. The other view is that each tax payer should pay taxes based on his or her ability (income) to pay.

9.2 TYPES OF TAXES

The international operations of a firm are broadly subject to three kinds of taxes. They are as follows:

1) Income tax or corporate tax
2) Withholding tax
3) Indirect taxes such as sales tax, excise duty, etc.

Income tax: This tax is levied on income generated by firm's operations. In developing countries, where the per capital income is low, corporate income tax generates a significant portion of government's revenue. The corporate income tax rate of some countries are given in Table 9.1.

Table 9.1: Tax Rate in Different Countries

Rank	*Economy*	*1 January 2003*	*1 January 2004*
Eleven highest			
1	Japan	42	42
2	United States	40	40
3	Germany	39.6	38.3
4	Italy	38.3	37.3
5	Canada	36.6	36.1
6	Israel	36	36
7	India	36.8	35.9
8	Malta	35	35
9	Pakistan	35	35
10	Spain	35	35
11	Sri Lanka	35	35
Eleven lowest			
1	Cyprus	10/15	10/15
2	Ireland	12.5	12.5
3	Estonia	0/26	0/26
4	Lithuania	15	15
5	Latvia	19	15
6	Hungary	18	16
7	Chile	16.5	17
8	Hong Kon (China)	16	17.5
9	Iceland	18	18
10	Slovakia	25	19
11	Poland	27	19

Source: World Investment Report, 2004.

Capital gains and losses occur due to local sale of capital assets. Capital assets are those assets which are not acquired in ordinary course of business, i.e. real estate, stocks and bonds, etc. Capital gains are usually taxed at lower tax rates than the corporate tax rates. Capital losses are allowed to be carried forward to be set off against capital gains in subsequent years.

Withholding taxes are the taxes imposed by the host government on dividend and interest payment to foreign investors and debt holders. These taxes are withheld by the paying corporation and paid to the government. The firm collects the tax on behalf of the government. For example, an Indian company has to pay interest of Rs. 10 lacs to foreign debt holders and withholding tax rate is 15%, the company would withhold an amount of Rs: 1.5 lacy and pay the same to the government.

Indirect taxes are those taxes in which the incidence is not on the firm, but it is responsible to collect the same and pay to the government. Sales tax may be levied ad valorem (on the value) or on the value addition (VAT) during a process of production. In England sales tax is levied when goods are wholesaled, in USA it is applied when goods are retailed. In India some states have adopted the Value Added Tax (VAT) system of sales tax collection.

Excise duty is the tax on the finished goods. This tax can be ad valorem (value based) or unit based (per unit tax).

9.3 TAX HEAVENS

A tax heaven country is one that has zero rate or very low rate of income tax and withholding tax. The distinguishing features of tax heaven are:

- Strict rules on secrecy and confidentiality with respect to business transactions.
- relative importance of banking and financial services in national economy,
- lack of currency controls,
- government measures promoting tax heavens.

The tax heavens can be grouped into four types:

1) Those having no income or capital gains tax
2) Those having a very low rate.
3) Those exempting all income from foreign sources from taxation.
4) Those allowing special tax privileges in specific cases.

The modus operandi of tax savings through tax heavens is as follows: MNCs have foreign subsidiaries operating into different tax environment. The MNCs create a 10 percent owned subsidiary in tax heaven which act as a corporate body where funds are repatriated from different subsidiaries. Tax heavens are a creation of tax deferral features on earned foreign income. In this way the MNCs are able to operate a corporate pool of funds for foreign operations without having to repatriate foreign earnings to the parent and in this way tax is saved.

9.4 INTERNATIONAL TAX MANAGEMENT STRATEGY

The minimisation of the overall tax b burden so as to maximise the overall profit is the strategy of an MNC. Firstly, the MNCs have to decide the quantum and timing of repatriation of profits from subsidiaries to the parent. If the subsidiaries are generating profits at a rate higher than that of parent it would be preferred not to repatriate profits, but in this case the parent MNC will not witness net cash flow thereby defeating the very purpose of investment:

Secondly, the tax burden can be minimised by judicious cost allocation between different units of the firm. If a firm allocates higher cost in a high tax country and show greater higher profit in low tax country the overall tax burden can be minimised. However, there are limits to cost allocations, specially when intermediate goods transferred from one country to another attracts custom duties.

The MNCs have to also decide upon whether the foreign operations should be in the form of a branch or subsidiary. If it is expected that during the initial year the foreign operations are going to incur losses it is better to operate through branches as branches do not represent an independent entity and so the loss incurred by one branch will be absorbed by profits of other units and the total tax burden would be lower.

The overall international tax strategy should be designed to avoid double taxation of income by two taxing countries. The tax treaties are designed to serve the following objectives:

- to prevent double taxation of the same income
- to prevent tax discrimination by local tax authorities
- to increase the predictability of tax incidence by specifying tax obligations
- to specify the type of tax subsidies.

Most of the double taxation relief treaties are based on the model proposed by Organisation for Economic Cooperation and Development (OECD). This model is called as `Draft Double Taxation Convention on Income and Capital'. This model was originally proposed in 1963 and revised in 1974,

9.5 THE MODES OF DOUBLE TAXATION RELIEF

Double taxation relief is generally granted by the country in which the parent company has its legal residence. The modes of double taxation relief are as follows:

1) Credit system without deferral
2) Credit system with deferral
3) Exemption
4) Deduction of tax paid abroad as expenditure
5) Investment Credit

In Credit system without deferral the taxes paid in the host country are allowed as a tax credit in the home country. For example, the tax rate in India is 35 percent and a foreign subsidiary of an Indian company pay taxes at the rate of 40 percent, the excess tax paid will be allowed to be offset against the amount of tax paid in the home country.

In credit system without deferral the taxation in the home country is deferred until earnings from the subsidiary are repatriated to the parent company. Profits of the subsidiary are taxed at the rate prevalent in the host country. They are subject to home country taxes only when they are repatriated.

In case of tax exemptions if the profits of the subsidiary are taxed in the host country, they are exempted from any taxation in the home country. This type of provision is prevelant in France and Netherlands.

A similar provision is that taxes paid in foreign country are treated as expenditure and allowed as deduction from total income in the home country.

In case of investment credit the amount of capital invested abroad is deducted from the income earned in the country of residence.

Transfer Pricing

Transfer pricing is a mechanism used by MNCs to price intracorporate exchange of goods and services so as to minimise taxes and maximise after tax profit. Transfer pricing involves charging of different prices for intracorporate transfers and sale to third parties for identical goods and services. The latter are called as arms length prices. Suppose a multinational petroleum company has a subsidiary in another country where taxes are high as compared to parent company's country. By supplying inputs at an inflated price the parent company will effectively increase post tax profit in low tax regime country and depress profit in high tax regime country thereby reducing the overall tax liability. Apart from tax savings transfer pricing may be used for one or more of the following:

1) Positioning funds at such locations which suits corporate working capital policies.

2) Reducing exchange rate exposure and circumventing exchange control restriction on profit repatriation.

3) Reducing custom duty payments and overcoming quota restriction in imports.

4) Window dressing of operations of subsidiaries.

9.6 INDIAN TAXATION SCENARIO

Taxes on Corporate Income

The Indian Government has its own taxation rules that influence the international business activities. The rules provide for both direct and indirect taxes. Tariff being an indirect tax is levied on imports. The rate varies form one commodity to the other.

The norms and rates of income tax vary depending upon whether a company is domestic or foreign and also whether a company is a resident assess or a non-resident assessee.

A domestic company is a company registered in India under the provisions of the Indian Companies Act and that declares its dividend in India. Others are treated as a foreign company. Again, a domestic company is treated as a resident assessee. On the contrary, a foreign company is treated as a resident assessee only when its entire operation, and not a part of it, is located in India.

The income is compartmentalised into (1) Indian income and (2) Foreign income. Indian income is an:

1. Income that accrues/arises in India and is received/deemed to be received in India.

2. Income that accrues/arises outside India but is received/deemed to be received in India.

3. Income that accrues/arises in Indian but is received/deemed to be received outside India.

Foreign income is an income that accrues/arises outside Indian and is received/ deemed to be received outside India.

A resident assessee is taxed on both its India income and foreign income. But a non-resident/foreign company is not taxed on its foreign income. There are, some foreign incomes which are treated as Indian income. Income of a business process out-sourcing (BPO) units in India, even if they are a permanent establishment of a non-resident foreign company, specific cases of interest, dividend, technical fees, royalty, etc. are apposite example. However, many of them are exempted from tax.

As far as the rate of corporate income tax is concerned, it varies between a domestic company and a foreign company. The Budget proposals for 2005-06 have brought down the tax rate from 35 per cent to 30 per cent alongwith a surcharge of 10 per net and education cess of 2 per cent in case of a domestic company. But in case of a foreign company, it is 40 per cent alongwith a surcharge of 2.5 cess for 2 per cent. The surcharge is applicable only after deducting rebate under Section 88E which deals with taxes on the transaction of corporate securities.

In case the tax liability of a company-domestic or foreign-is less than 7.15 per cent (plus surcharge) of the book projects, the book profits are deemed to be the total income chargeable to tax at the rate of 7.5 per cent plus surcharge which is known as minimum Alternate Tax (MAT). Presently, a credit is allowed for MAT that will be available in the next five years.

If one probes the burden of corporate income tax of a domestic company vis-a-vis a foreign company, it is evident that foreign company has to bear a lower tax burden.

Domestic Company	*Foreign Company*
Income tax @ 30%	Income tax @ 40%
Surcharge @ 10%	Surcharge @ 2.5%
Education Cess @ 2%	Education cess @ 2%
Tax on dividend assuming	
90% distribution @ 9.34%	Total @ 41.82%
Total @ 42.0%	

Since dividend distributed by a foreign company is exempt from tax, the Budget 5-06 lowers the tax burden of a foreign company. The various income tax deductions available to the companies are as follows:

Section	*Nature of deduction*
80G	Donations to charitable institutions and funds.
80GGA	Donations for scientific research for rural development.
80HHB	Profits and gains from projects outside India.
80HHEA	Profits and gains from housing projects.
80BHC	Profits and gains from export turnover.
80HHD	Earnings in convertible foreign exchange.
80HHE	Profits from export of computer software.
80HHF	Profits from export of film new industrial undertakings.
80-I	Profits and gains from new industrial undertaking.
80-IA	Profits and gains from industrial undertaking engaged in infrastructure, etc.
80-IB	Profits and gains from certain industrial undertaking other than infrastructure development undertaking.
80JJA	Profits from the business of collecting and processing of bio-degradable waste.
80JJAA	Employment of new working.
80-0	Royalty received from foreign enterprises.

9.7 FEMA: AN INTRODUCTION

There is a German word zeit-geist, meaning `spirit of time'. Nothing better describes the evolution of foreign exchange regulation in India. The history of foreign exchange control and regulation can be traced back to World War II, during which there was a

shortage of foreign exchange resources. To overcome this a system of exchange control was first time introduced through a series of rules under the Defence of India Act, 1939 on temporary basis. Soon after independence a complex system of controls were imposed for all external transactions through a legislation i.e. Foreign Exchange Regulation Act (FERA), 1947. These controls were further tightened through FERA, 1973. These restrictions continued till mid 1990s when relaxations were made in the operations of FERA, 1973. The control framework of FERA, 1973 was mainly transaction based in which all transactions in foreign exchange were prohibited, unless specifically permitted.

After the upheavals of early 1990s the process of economic stabilization and structural reforms gathered momentum. The agenda for changes in foreign exchange regulations were initiated by the report of High Level Committee on Balance of Payments (Chairman Dr. C. Rangarajan) 1993. The main recommendations of the Committee were as follows:

1) Introduction of market determined exchange rate regime.
2) Liberalisation of current account transactions leading to current account convertibility.
3) Compositional shift in capital flows away from debt creating to non debt creating flows.
4) Strict regulation of external commercial borrowings especially short term debts.
5) Discouraging volatile elements of flows.
6) Full freedom for outflows associated with inflows (i.e., principal, interest, dividends profit and sales proceeds).

In 1993 the exchange rate of rupee was made market determined and in August 1994, India accepted Article VIII of the Articles of Agreement of the International Monetary Fund and adopted the current account convertibility.

The Foreign Exchange Management Act, 1999 (FEMA) has been enacted to consolidate and amend the law relating to foreign exchange with the objective of facilitating external trade and payments and for promoting the orderly development and maintenance of the foreign exchange market in India. It replaces the Foreign Exchange Regulation Act, 1973 except as provided in 9 hereunder. FEMA has come into effect from June 1, 2000.

With the coming into effect of FEMA India will have moved from a regulatory mechanism to a management mechanism with respect to foreign exchange. It is a great change not only structurally but also psychologically.

9.7.1 Broad Scheme of the FEMA

Section 3 - Prohibits dealings in foreign exchange except through an authorised person. This Section says that no person can, without general or special permission of the RBI

a. Deal in or transfer any foreign exchange or foreign securities to any person not being an authorised person (corresponding to sections 8 and 19 of FERA).
b. Make any payment to or for the credit of any person resident outside India in any manner (corresponding to section 9(1)(a) of FERA).
c. Receive otherwise through an authorised person, any payment by order or on behalf of any person resident outside India in any manner (corresponding to section 9(I) (b) of FERA) and
d. Enter into any financial transaction in India as consideration for or in association with acquisition or creation or transfer of a right to acquire, any asset outside India by any person (corresponding to sections9(1)(f) & (g) of FERA).

Section 4 - restrains any person resident in India from acquiring, holding, owning, possessing or transferring any foreign exchange, foreign security or any immovable property situated outside India except as specifically provided in the Act.

Section 6 -deals with capital account transactions. This section allows a person to draw or sell foreign exchange from or to an authorised person for a capital account transaction.

Section 7 - deals with export of goods and services. Every exporter is required to furnish to the RBI or any other authority, a declaration etc. regarding full export value.

Section 8 - casts the responsibility on the persons resident in India who have any amount of foreign exchange due or accrued in their favour to get same realised and repatriated to India within the specific period and the manner specified by RBI.

Section 10 and 12 - deals with duties and liabilities of the Authorized persons. Authorised person has been defined in Sec.2(c) of the Act which means an authorised dealer, money changer, off shore banking unit or any other person for the time being authorized to deal in foreign exchange or foreign securities.

Section 13 anti 15 - of the Act with penalties and enforcement of the orders of Adjudicating Authority as well power to compound contraventions under the Act.

Section 36 to 37 - pertains to the establishment of Directorate of Enforcement and the powers to investigate the violation of any provisions of Act, rule, regulation, notifications, directions or order issued in exercise of the powers under this Act. The Director of Enforcement and other officer of Enforcement not below the rank of Asstt. Director have been empowered to take up investigations.

Primarily there are no restrictions on current account transactions related to foreign exchange and a person may sell or draw foreign exchange freely for his current account transactions, except in a few cases where caps have been prescribed (Section 5).

Capital account transactions, though freed to a great extent, continue to be regulated by RBI, who will lay down the provisions as regards the extent of prohibition, restriction, and regulation (Section 6). But there are two very important areas on which RBI cannot Impose any restrictions viz. drawing of foreign exchange for the repayment of any loans and for depreciation of direct investments in the ordinary course of business.

IMPORTANT TERMS UNDER FEMA

Capital Account Transaction means a transaction which:

* Alters foreign assets and foreign liabilities (including contingent liabilities) of Indian residents.
* Alters Indian assets and Indian liabilities of Non-residents.
* Specified transactions listed in section 6(3).

Investments, cross border loans and transfer of wealth across borders. RBI has been empowered to regulate the capital account transactions. Unless the transaction is permitted as per the regulations, foreign exchange cannot be drawn for the same.

Current Account Transaction means all transactions, which are not capital account transactions, Specifically it includes:

* Business transactions between residents and non-residents. Short-term banking and credit facilities in the ordinary, course of business.
* Payments towards interest on loans and by way of income from investments.
* Payment of expenses of parents, spouse or children living abroad or expenses on their foreign travel, medical and education.

* Gifts.

Some principles which can be considered to distinguish between capital and current account transactions are:

* If a transaction gives rise to any claim or obligation between a resident and a non-resident it is a capital account transaction, e.g. if machinery is purchased on hire by a resident from a non-resident he is obligated to the non resident.

* If on execution of a transaction there are no outstanding financial obligations, then it is a current account transaction, e.g. if a non-resident purchases machinery and pays for the same in cash, there is no further financial obligation between the resident and non-resident. This is current account transaction.

The Central Government has the power to regulate the current account transactions. Unless the transaction is restricted, foreign exchange can be drawn for the same. See para 16 for restrictions on current account transactions.

9.7.2 Important Features of FEMA

INVESTMENTS ABROAD BY INDIAN RESIDENTS

Joint Ventures Abroad

RBI has been granted powers to permit Indian investments abroad in Joint Ventures (JV) and Wholly Owned Subsidiaries (WOS). Investments can be made under the automatic route, in which case prior permission is not required, or the non-automatic route, in which case prior permission is required. There are various options available for investment under both the routes. General Guidelines:

1. Indian companies and partnership firms registered under the Indian Partnership Act, 1932 are allowed to invest abroad. Individuals (except under ESOP schemes or by way of qualification shares to act as Directors), HUFs, AOPs, etc. are not allowed to invest abroad.

2. Investments can be made in existing companies or new companies or for acquiring overseas business.

3. The foreign entity can be engaged in any industrial, commercial, trading, service industry, financial services such as insurance, mutual funds, etc.

4. Following activities are not permitted:

* Portfolio Investment by Indian parties.
* Investment in banking and real estate sectors.

5. Investment can be in equity, debentures, loans, or by way of guarantees. Guarantees are considered @ 50% of the value to consider investment limits.

6. Remittance can be by way of cash, or export of goods and services. For contribution by way of exports, no agency commission will be payable to the wholly owned subsidiary/Joint Venture company.

7. Investment under automatic route will not be permitted to parties on RBI Caution List, or who have defaulted to the banking system in India and whose names appear on the Defaulter's list.

8. Investment under automatic route is not available where it is proposed to set up a holding company or a special purpose vehicle which in turn will set up one or more step down subsidiaries as operating units.

9. Dividends, royalties, etc. due to Indian investor should be repatriated to India in accordance with the prevailing time limits.

10. Authorised dealers have been permitted to release offering exchange for feasibility studies prior to actual investment.

11. In the event of changes proposed in the JV (where the Indian Party's investment exceeds 50 %)/WOS regarding activities, investment in another concern/subsidiary or alterations of share capital, there are approvals/reporting, requirements from/to RBI. However, these are relaxed for investments made entirely out of EEFC Accounts or by utilizing ADR/GDR proceeds.

Euro issues, ADR/GDR Issues

* No end-use restrictions except prohibition on investment in stock market and real estate

* A broker can purchase shares on behalf of Non-Residents and convert the shares so purchased into ADR/GDR

* Two-way fungibility allowed in case of ADR/GDR issues; i.e., ADR/GDR can be converted into underlying equity shares in India and shares already issued in India can be converted into ADR/GDR and issued abroad.

Technical know-how fees and royalty

Fees can be remitted without RBI permission, on automatic approval basis, up to US $ 2 million in lump sum. Further royalty @ 5% on domestic sales, and @ 8% on export sales can be paid over 7 years from commencement of production or 10 years from the date of agreement (net of taxes), whichever is earlier. Wholly owned subsidiaries can make payments for royalty and know-how payments subject to 5% or 8% limits as above. However there is no restriction on duration of royalty payment.

Royalty payment for trademarks and brands

Royalty up to 2% of net export sales and 1 % for net local sales is allowed to be paid to the foreign collaborator under the automatic route for use of his trademarks and brand name even if there is no transfer of technology.

Foreign Institutional Investors (FIIs)

FIIs such as Pension Funds, Investment Trusts, Asset Management Companies, etc., who have obtained registration from SEBI, are permitted to invest on full repatriation basis in the Indian Primary and Secondary Stock Markets (including OTCEI) as well as in unlisted, dated Government Securities, Treasury Bills and Units of Domestic Mutual Funds without any lock-in period.

Limits on Investment in the Primary and Secondary Markets are:

a. The total holdings of all FIIs in any company will be subject to a ceiling of 24% of its total issued capital. The company concerned can raise this ceiling of 24 % up to the sectoral cap/statutory ceiling as applicable.
b. A single FIT cannot hold more than 10% of the issued capital of any company. But no FII shall purchase shares or convertible debentures of an Indian Company engaged in the print media sector.

EXTERNAL COMMERCIAL BORROWINGS (ECB)

Any legal entity can raise money abroad through the ECB route as follows:

A. Automatic Route:- Fresh ECB or refinancing of existing ECB with average maturity of not less than 3 years for an amount up to US $ 50 million, subject to conditions laid down in Schedule H. Three copies of the agreement will have to be filed with the Regional Office of the RBI after signing the ECB agreement.

B. Raising ECB in excess of US $ 50 million but up to US $ 100 million apply to the RBI for permission.

C. Raising ECB in excess of US $ 100 million will be considered by the Government of India.

Applications in all the above cases has to be made in Form ECB.

Pre-payment of ECB is permitted by utilization of funds available in the EEFC Account of the borrower. For this purpose, borrowers can make application to RBI and they will be permitted to credit higher than the normally permitted percentage of export proceeds to their EEFC Account.

BORROWINGS THROUGH LOANS/DEPOSITS

Indian companies are now permitted to accept deposits from NRls/PIOs/OCBs on repatriation or non-repatriation basis subject to certain conditions.

Indian proprietary concerns and firms are permitted to accept deposits from NR1s/ PIOs on non-repatriation basis subject to certain conditions.

Resident individuals are permitted to avail of interest free loans up to US $ 2,50,000 from their NRIs/PIOs relatives on non-repatriation basis subject to certain conditions.

Proprietary concerns and partnership firms are permitted to avail of interest' bearing loans *from* NRIs/PIOs on nonrepatriation basis subject to certain conditions.

Special permission of the RBI will be required in case where deposits/loans do not fulfil the specified criteria or where the deposits/loans are on repatriation basis in the case of individuals, proprietary concerns and firms.

Both residents and non residents can open a bank account in India. The type of bank accounts and their main features are given in Tables 9.land 9.2 respectively.

Table 9.1: Types of Deposit Schemes for Non Resident

Particulars	*(Foreign Currency Non-Resident Account (FCNR A/c)*	*Non-Resident External Rupee Account (NRE A/c)*	*(Non-Resident Ordinary Account (NRO A/c)*
Who can open an account Joint accout more non-resident	NRIs or OCBs In the names of two or more non-resident individuals	NRIs or OCBs outside India In the names of two or more non-resident · individuals	Any person reident May be held jointly with residents
Nomination	Permitted	Permitted	Permitted
Currency in which account denominated	Pound Sterling, US Dollar, Jap. Yen, or Euro.	Indian Rupees	Indian Rupees
Repatriability	Repatriable	Repatriable	Not repatriable except for the following in the account 1. Current income and interest 2. Upto US$ 1 million per calendar year for any bonafide purposes out o. NRO balances/ sales proceeds of assets
Type of Account	Term Deposits only	Savings, Current, Recurring, Fixed Deposit	Savings, Current, Recurring, Fixed Deposit
Period for fixed deposits	For terms not less than 1 year and more than 3 years	No restriction	No restriction
Rate of Interest	Subject to cap: LIBOR - 250 basis points	Subject to cap: LIBOR/SWAP+100 basis points	Banka are free to determine interest rates.

Table 9.2: Features of various foreign currency deposit schemes available to Resident Indians

Particulars	*Resident Foreign Currency Account (RFC Account)*	*Resident Foreign Currency (Domestic) Accout (RFC(D)*	*Exchange Earner's foreign Currency Accout (EEFC Account) Account)*
Who can open an account	Any person resident in India.	Resident Individuals	Any person resident in India
Sources of Funds	1. Foreign exxhange received as pension/ superannuation /other benefits from employer aboad 2. Resaslisation of assets held abroad 3. Foreign exchange acquired as gift or inheritance form person who was NRI	Foreign exchange acquired: 1. While on a visit aboad 2. from any person on visit to India or honorarium or gift or for service or settlement of any lawful obligation 3. by way of honorarium or gift while on a visit abroad 4. representing unspent foreign exchange acquired during travel abroad 5. as gift from a close relative 6. by way of earning through export of goods/services or as royalty honorarium or by any other lawful means. 7. representing the disinvestment proceeds received by the resident a/c holdere on conversion of shares held by him to ADRs/GDRs under the sponsored ADR/GDR scheme approved by the FIPB of Govt. of India.	A 100% Export Oriented Unit or a nit in (a) Export processing zone or (b) Sortware technology park or (c) Electronic hardware technology park may credit upto 100% and any other person resident may credit upto 50% of theeir foreign exchange earnings. (d) Professional like scientists, professors of Indian Universities, economists, lawyers, doctor, artists, architects, engineers, consultants, Cost/Chartered Accountants, Directors of Boards of overseas companies etc. who render services in their individual capacities outside India, may credit upto 100% of their earnings.
Joint account of two or more residents	Not permitted	Not permitted	Not permitted
Joint account with NRI	Not permitted	Not permitted	Not permitted
Types of account	Savings Current Fixed Deposit	Current Account	Current Account
Period for fixed deposits	Like any resident	N.A.	N.A.

9.8 SUMMARY

The financial decisions of MNCs, such as international investments, dividends, repatriation of profits etc. are based on the tax structure in the host country. MNCs have to mainly pay three types of taxes in the host country, viz. income tax, witholding tax and indirect taxes, such as sales tax and excise duties.

There are some countries which have a negligible tax rate and no restrictions on currency movements. These type of countries are known as tax heavens. Most of the MNCs establish their subsidiary in these countries and this subsidiary act as an intermediary between the parent company and the subsidiaries in other host countries.

Since the profits of the MNC's subsidiary are taxed in the host country as well as home country, most of the countries have entered into double taxation relief treaties as a result of which the profits are taxed either in the host or the home country.

In India foreign exchange transactions are regulated by Foreign Exchange Management Act.

9.9 SELF ASSESSMENT QUESTIONS

1) What should be the key features of International Tax system?

2) What are the various types of taxes which an MNC has to pay?

3) Explain in brief the meaning of Tax Heavens.

4) Explain about the various modes of double taxation relief.

5) Explain in detail the Indian tax scenario.

6) Explain in detail the broad scheme of FEMA.

7) Explain in detail the important features of FEMA.

9.10 FURTHER READINGS

Price Waterhouse: Guide to tax laws, Bantam Books, New York, 1986.

Price Waterhouse Corporation Taxes, A worldwide summary, Price Waterhouse, New York, 1987.

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